

THE
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NAVY GRADUATE COMPTROLLERSHIP PROGRAM

A CURRENT VIEW
OF THE
PERFORMANCE BUDGET

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For
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PREFACE

To some of us in the Navy who had been concerned more with doing our own little job and less with overall Naval policy, the present performance type of budget appeared on the scene relatively unheralded.

Because of the expectations for a better Navy resulting from this planning-budgeting-management tool, I have chosen to do this paper to knit together in a fashion indicated by the title, some information concerning the performance type budget.

Informative writings on the performance type budget are still not plentiful. Various writings place the "credit" for our having such a budget in divers quarters. Members of the naval establishment may take pride in the fact that the United States Navy may well be the leading organization in terms of having fathered the performance type budget. These general statements will be treated at greater length later, herein.

It is generally known that the Commission on Organization of the Executive Branch of the Government, now known as the first Hoover Commission, was established by unanimous vote of the Congress on July 7, 1947 by Public Law 162 of the 80th Congress. The great breadth of the field to be examined was such, that any less ably organized group might have easily failed. Mr. Hoover,

however, wisely made use of various so-called task-forces to explore the numerous fields to be examined. The written reports of the many task forces generally constituted the basis for reports of the Hoover Commission. When it came to the Commission Report on Budgeting and Accounting,¹ however, Mr. Hoover himself personally undertook its preparation because of his strong belief in its extreme importance.² It was also Mr. Hoover who personally chose the expression "performance budgeting." He made the choice of this term to signify the end product in financial planning because it implies a systematic approach to the selection and depiction of government work through programs. For this reason it is often referred to, and rightly so, as a program budget.³ These expressions are synonymous with functional and activity budgets.⁴ In my study of the works listed in the bibliography, I found the performance budget referred to interchangeably as program budget, activity budget or functional budget. I shall use Mr. Hoover's term herein, but the other expressions encountered as above all refer to the same instrument.

¹The Commission on Organization of the Executive Branch of the Government, Budgeting and Accounting, (Washington: Government Printing Office, February 13, 1949).

²Robert L. L. McCormick, The Future of Program Budgeting, A progress report by Robert L. L. McCormick, Research Director of the Citizens Committee for the Hoover Report (Washington: Unpublished mimeographed release to press found in Bureau of Budget Library, May 29, 1950), p.2.

³Arthur E. Buck, "Performance Budgeting for the Federal Government," Tax Review, X(July, 1949), 34.

⁴Walter G. Held, "Performance Budgeting in Municipalities," GRA Reporter, III (May-June, 1951), 2.

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CHAPTER I

INTRODUCTION - ADUMBRATIONS OF THE PERFORMANCE TYPE BUDGET

The Hoover Commission stated as follows, "We recommend that the whole budgeting concept of the Federal Government should be refashioned by the adoption of a budget based upon functions, activities, and projects; this we designate as a "performance budget."⁵ In the discussion which followed, it was stated, "The idea of a performance budget is not new. It has been adopted in the modernization of budgets by some States and several municipalities."⁶ To most persons it would surely appear that a performance budget is new - there is certainly a dearth of written material on the subject. It is hoped that this paper will serve to set down in one place something drawn from the limited material now in print concerning the performance budget.

The first "modern" recorded mention of the performance budget appeared in the actual Task Force Report on "Fiscal, Budgeting and Accounting Activities." This is the report of the Task Force group to the whole Hoover Commission and is sometimes supplied as Appendix F to the actual Commission Report.⁷ The earliest

⁵The Commission on Organization of the Executive Branch of the Government, op. cit., p.8.

⁶Ibid., p.9.

⁷Ibid.

"modern" recommendation for a Federal Performance Budget appears in this Task Force Report in Part Three in the "Report on Federal Budgeting" prepared by A. E. Buck for the Institute of Public Administration of New York (under contract to the Hoover Commission). Please note also the recommendation which precedes the actual Performance Budget recommendation:

2. The Budget should be submitted to Congress on April 1st or thereabouts, the detailed expenditure estimates having already been sent to the appropriations committees. By adopting a program or performance budget, this date is entirely feasible without hampering in the least the work of the committees on appropriations.

3. A program or performance budget should be substituted for the present budget, thus presenting in a document of much briefer compass the Governments' expenditure requirements in terms of services, activities, and work projects rather than in terms of the things bought. Such a budget would not detract from congressional responsibility and should greatly improve and expedite committee consideration.⁸

(Underscoring in paragraph 2. above is mine to indicate first mention of subject).

The tenor of recommendation number 2. above, together with a study of the rest of Mr. Buck's section on Federal Budgeting shows that a prime consideration in his recommending the performance budget, was to enable presentation to Congress of a manageable, intelligible document, at a time close to the beginning of the fiscal year which the document concerns, (i.e. present the

⁸Task Force Report on, Fiscal Budgeting and Accounting Activities, prepared for the Commission on Organization of the Executive Branch of the Government (Sometimes supplied as Appendix F to Number 5 above), (Washington: Government Printing Office, January 15, 1949), p.43.

expenditure estimates to Congress on about April 1st, instead of in early January.⁹ He was equally motivated toward recommending the ".... [performance budget] document of much briefer form....,"¹⁰ submitted later in the year, as a means of avoiding the situation we have in those years when a new President takes office. In those cases the "old" President submits the budget estimates in January for the fiscal year which his successor will "inherit". (It is recognized of course that the successor is able to modify in some degree). We shall examine in a rough way, later, herein, how adoption of the performance budget by one department has affected its briefness in the budget document.

On the subject of the "....idea of a performance budget is not new....",¹¹ Dr. Rowland Egger, then Director of the Bureau of Public Administration of the University of Virginia and an assistant to the Task Force on Fiscal, Budgeting and Accounting of the Hoover Commission, had this to say:

It is to be noted that the Commission's shiny new word "performance" budget represents a return to, rather than a departure from, congressional thinking underlying the Budget and Accounting Act of 1921. As Representative Good remarked in the case of the house debate on the measure, "we do not appropriate dollars for the purpose of making appropriations; we appropriate dollars to carry out work planned for the government. [Dr. Egger's scoring]. The plain fact seems to be that in the struggle to "get back to normalcy" in the early years of the 1920's, the Bureau of the Budget and the Congress never found time to shift their approach to budgeting, away from the "appropriation pivot" around which it had revolved

⁹Ibid., pp. 35-84.

¹⁰Ibid., p. 43.

¹¹Ibid.

for many decades prior to 1921, to a "government work program" basis, which was implicit in the Act from the very beginning. Thirty years later we discover a new basic principle on which the original act was built, a principle which was itself plagiarized from Frederick Cleveland's work for Mr. [William Howard] Taft's Commission on Economy and Efficiency a decade before.¹²

All due respect to Dr. Egger's testimony, even today we just don't see or hear a great deal about a performance budget. Getting down to concrete cases, it does appear that in preparing the expenditure estimates for the Borough of Richmond, New York City (this is actually Staten Island) for 1913-1915, "cost data" budgeting was used in the public works segment of the document. The idea was sound, but resulting legislation included so many administrative details that the attempted shift foundered.¹³

¹²U. S. Congress, Senate, Committee on Expenditures in the Executive Departments, To improve Budgeting, Accounting and Auditing Methods of the Federal Government, Hearings before the Committee on S. 2054 and Amendments, Feb. 27, 28, March 2, 3, 6, and 7, 1950, 81st Congress, 2nd Session, (Washington: Government Printing Office), pp. 141-142.

¹³Contra Costa County Taxpayer's Association, An approach to the Technique of performance budgeting, Research Bulletin Number 10, (Martinez: California, 1952), p.2.

CHAPTER II

THE PERFORMANCE BUDGET MOVEMENT GROWS

Although performance budgeting was probably on the way anyway as we shall see later herein, the largest group of people learned about the performance budget through the medium of the publicity given the many fine recommendations of the Hoover Commission, by the Citizen's Committee for the Hoover Report. Shortly after the Hoover Reports, some scattered writings touched on the performance budget. Some of these writings stated that certain local governmental entities were on the performance budget. One such paper listed the following municipalities as having successfully prepared performance budgets in 1950:

Oxnard, California, pop. 18,979
Richmond, Virginia, pop. 193,043
Kansas City, Missouri, pop. 399,178¹⁴

The following were also listed as having developed, in varying degrees, aspects of performance budgets in 1950:

San Diego, California, County, pop. 627,010
Los Angeles, California, County, pop. 4,466,000¹⁵

A study of the actual budget for Oxnard, California for 1952-'53 shows that the major reason that it is referred to above as a

¹⁴Ibid., p.3.

¹⁵Ibid.

performance budget is because of the inclusion of this sentence, "Accompanying each of these [estimates of expenditures by object classification] is a description of the functional work program that is to be accomplished by each department."¹⁶ The sole functions actually priced in the entire budget were: street maintenance, street curbing, refuse collection, street lighting and weed control.¹⁷ All other departments merely listed expenditures estimates by object classifications, thus falling far short of what a performance budget has come to mean to me.

In the wake of the Hoover Report, more interest was shown in performance budgeting than ever before. In 1950, the state of Oklahoma issued instructions for preparation and presentation of a performance budget.¹⁸

An Oregon "Little Hoover" committee issued a first report which saw fruition in a 1951 Oregon Law which directed a study and review of state budgeting practices. The resulting study did not go "overboard" in advocating a performance type budget but instead very carefully considered the matter and "...recommended for Oregon a ...[performance budget]...for a "whole" viewpoint rather than [a budget emphasizing] detail and means."¹⁹ Again in Oklahoma,

¹⁶City of Oxnard, California, 1952-'3 Budget, Prepared by the Office of the City Manager, Presented to the City Council, April 15, 1952, p.3.

¹⁷Ibid., p.49.

¹⁸State of Oklahoma, Division of the Budget, Preparation of the Budget, (Oklahoma City, Oklahoma: 1950), pp. 1-20.

¹⁹State of Oregon, Division of the Budget, The Performance

an article appeared in early 1950 which outlined budget advances in the three years since that state enacted its first budget law in 1947. The article described machine tabulation as it was then used to keep record of figures that had not been available before that time. The next forward step described were plans to go on to a performance budget.²⁰ In 1952, it was reported that the City of Los Angeles, California had installed the performance type budget in all departments except Airport, Harbor, Water and Power departments.²¹ At that time Los Angeles had progressed enough to assert that the performance budget reporting system which they viewed as a logical follow-up of their performance budget, was making possible:

(1) Provision of timely data to aid in making any necessary adjustments in personnel assignments necessitated by [changing] work loads.

(2) Provision of information for reviewing the execution of departmental programs.

(3) Provision of factual work measurement data.

(4) Provision of basis for determining "before and after" effects of procedural and organizational changes for promotion of maximum effectiveness in personnel organization.²²

Budget (Budgetary Improvement in Oregon State Government), A report submitted to the Governor, (Salem, Oregon: December 1, 1952), pp. 1-19.

²⁰Steve Stahl, "The Performance Budget In Oklahoma", GRA Reporter, II (March - April, 1950), 1-3.

²¹City of Los Angeles, California, City Administrative Officer, Performance Budget Reporting Procedure of the City of Los Angeles, (Los Angeles, California: 1952), pp. 1-11.

²²Ibid.

One of the very best performance budgets discovered was evidenced in a Quarterly Budget Report of the Village of Wayne, Michigan as early as 1948. Under public works, to cite one specific case of the many similar examples contained in that report, the following line appears under a long tabulation of many other "activities":

<u>Activity</u>	<u>Work Unit</u>	<u>No. Units</u>		<u>Man Hours</u>		<u>Cost</u>	
		<u>Budg- eted</u>	<u>This Period</u>	<u>Budg- eted</u>	<u>This Period</u>	<u>Budgeted</u>	<u>This Period</u>
Asphalt Crack Filling	Gals. Asphalt	4,000	1,824	400	183-1/3	1,832.26	714.16 ²³

As some governing entities were installing and using the performance budget to varying degrees as shown, citizen groups in New York City,²⁴ Milwaukee,²⁵ Utica,²⁶ and elsewhere were calling attention to inefficiencies of the present (old) budgeting methods, citing rising costs of government and asking for the performance budget as a tool for better and more efficient government.

Now, although the Hoover Commission stated "...that the performance budget was not new and [had] been adopted by some states and municipalities...", my rather exhaustive study shows that the performance budget might not have been new, but it was surely far from being really well known.

²³Village of Wayne, Michigan, Quarterly Budget Report for Quarter Ending Sept. 30, 1948, (Village of Wayne, Michigan: Sept. 30, 1948), p. 29.

²⁴Anon., The Searchlight, Published by Citizens Union of the City of New York, XLI, No. 3, (New York City: Sept., 1951), 1-3.

²⁵Citizens Governmental Research Bureau of Milwaukee, Performance Budgeting, Bulletin Series of Citizens Governmental Research Bureau of Milwaukee, XL, No. 16, (Milwaukee, Wisconsin: 1952), 1-7.

²⁶Municipal Research Bureau of Utica, N. Y., The Performance

Budget, Bulletin Series "Its Your City", No. 21, (Utica, New York: 1950), 1-3.

CHAPTER III

APPEARANCE ON THE FEDERAL SCENE

The performance budget first seems to have appeared on the Federal scene in 1937 in the Department of Agriculture, where a uniform project system was installed in some bureaus. This system definitely had the performance budget approach.²⁷

The next appearance of the performance budgeting approach at the Federal level came in January, 1947, when the Department of the Navy, submitted its fiscal year 1947-'48 expenditure estimates in two formats; one was the conventional method, the alternative method was on a performance basis.²⁸ This action was taken by the Navy in response to a request made in January, 1946, by the Chairman of the House Sub-Committee on Naval Appropriations, for a revised Navy budget that would clarify management and fiscal responsibilities of the Navy. The purpose behind the request was an overhauling of the naval appropriation structure.²⁹

²⁷Don S. Burrows, "A program approach to Federal Budgeting", Harvard Business Review, XXVII (May, 1949), 281.

²⁸Chas. A. Blick, "Performance Budget for the Department of the Navy", Bureau of Supplies and Accounts Monthly Newsletter, XIV (Feb., 1950), 5-6.

²⁹U. S. Department of the Navy, Office of Budget and Reports, Concept of the Navy's 1951 Performance Budget, (Washington, D. C.: Feb., 1950), p. 2.

The conventional budget for the fiscal year 1948 had 61 appropriations whereas the alternate form had 31 appropriations. The difference in number of appropriations resulted from:

(1) The 21 appropriations for salaries in Washington, D. C. (19 Navy, 2 Marine Corps) were combined with the major programs which they supported, and,

(2) Many appropriations for training and education under the Bureau of Naval Personnel were combined or became parts of other appropriations, thereby reducing their number by nine.³⁰

It has been pointed out that the U. S. Naval Hospital, Bethesda, Maryland, under the conventional '48 budget, was run by 12 appropriations from 8 bureaus of the Navy Department. However, under the alternate form, Bethesda Naval Hospital would have been run on 4 appropriations from two bureaus of the Navy Department.³¹ The Navy held at that time that the following advantages would accrue from the use of the alternate form (performance budget):

(1) Fiscal Management would parallel management responsibility.

(2) Internal management would be less complex.

(3) Fiscal control would be facilitated.

(4) Budget presentation would be more effective.³²

³⁰Blick, op. cit., XIV, 5.

³¹60 Stat. 481-495: The Budget of the United States Government for the Year Ending June 30, 1948, (Washington, D. C.: Government Printing Office, 1947), pp. 689-725.

³²Department of the Navy, Proposed Revision of the Naval Appropriation Act, Nav Exos 13048, a Navy Department Publication, (Washington, D. C.: Dec., 1946).

In January, 1947, when the alternate form of expenditure estimates was presented to Congress, there had been a change in party control and inasmuch as many members of the Appropriations Committee of the House were new, the Sub-Committee decided to consider the budget only on the basis of the old structure.³³

This situation gave rise to an interesting exchange two years later between Congressman Harry R. Sheppard of California, and Rear Admiral Hopwood, Navy Director of the Budget. Congressman Sheppard was a minority member of the sub-committee when the alternative form was presented in January 1947, and at the time of this exchange two years later, was a majority member of the sub-committee. He inquired of Admiral Hopwood what the basic thinking was two years earlier when the alternate form of the Navy expenditure estimates was not considered, to which Admiral Hopwood replied:

It was that with the change of administration and the lack of time for the committee to study and have a thorough understanding of such a radical change in budget structure, that it was decided to defer it until later.³⁴

To which Congressman Sheppard made this succinct reply:

As far as educating the committee was concerned, it would [have been] a lot more simplified to take the later case [go to the alternate form], than to take a new man and put him

³³Chas. L. Kelchner, The Development of a Performance Budget for the Department of the Navy, (Washington, D. C.: Thesis-American University, 1950), pp. 55-59.

³⁴U. S. Congress, House, Committee on Appropriations, 81st Congress, 1st Session, Hearings on National Military Establishment Appropriation Bill for 1950, (Washington, D. C.: Government Printing Office, 1949), p. 974.

through the old [budget form], at least that is my analysis.³⁵

The Navy alternate form in 1947 did not, however, go un-noticed by any means as the Senate said:

The Committee has noted the submission of the alternate budget which is designed to: Provide fiscal responsibility, paralleling management responsibility, simplified internal management, facilitate fiscal control, greater clarity in budget presentations and improvement of personnel control. The Committee endorses these objectives.³⁶

With the foregoing background in mind, it is interesting to consider a report of the Eberstadt Task Force on National Security Organization contained in the Hoover Report, "The Committee found "...extravagance in military budgets and waste in military expenditures which show a serious lack of understanding of the effect of military costs and spending upon the total economy."³⁷ This report crystallized an impression I received from reading the entire Hoover Report,³⁸ and that is, that responsible civilians both in and out of government appeared afraid of we people in the military because of the way in which we spend money. When so many responsible people have that feeling, it certainly behooves us in the military to continually do the very best with the littlest possible. Consider further a

³⁵Ibid.

³⁶U. S. Congress, Senate, Committee on Appropriations, 80th Congress, 1st Session, Report No. 330 on Navy Department and Naval Service Appropriation Bill for Fiscal Year 1948, (Washington, D. C.: Government Printing Office, 1947), p. 5.

³⁷The Hoover Commission Report, U. S. Commission on Organization of the Executive Branch of the Government, (New York, McGraw-Hill Book Co.: ca, 1950), p. 187.

³⁸Ibid.

passage from a relatively less known report:

Our military budget system has broken down...the [appropriation structures] do not permit ready comparisons, they impede administration, and interfere with the efficiency of the military establishment. Congress allocates billions of dollars without accurate knowledge as to why they are necessary and what they are being used for...³⁹

What we have seen in the last decades, is a growth of Government of such magnitude that by 1949 people experienced difficulty in comprehending its size and/or scope of functions. Many departments and entities that originally had a single, simple, function, had by then bloomed into vast organizations performing a multitude of functions. Not the least of these is our own department which has at one time or another entered into many fields of which a fraction of a percent are: roasting coffee, making clothing, building houses, and running retail stores. With the desire to control the operations of this variety of activities, it is natural that control should be by means of that single common denominator -- dollars. But the structure in which those dollars had traditionally been viewed, had become incomprehensible, witness Congressman Sheppard's remark previously quoted herein.

A means of comprehending the dollar denominator was held out in the performance budget. Many authorities could well be quoted on what a performance budget is, but suffice it to quote only Mr. Frederick J. Lawton, Director of the Bureau of the Budget in 1950:

³⁹Committee on the National Security Organization, Report to the Committee on Organization of the Executive Branch of the Government, II Unpublished mimeographed report, filed with Hoover Commission Reports, National Archives, (Washington, D. C., Nov. 15, 1948), 149.

In the performance budget, what you would have as a primary classification would be operations (functions) that the Veterans Administration conducts.

What is of interest to Congress, we feel, is how much the Veteran's Administration is spending to run the G. I. Bill, how much it is spending for insurance, how much it is spending for hospitalizing veterans...

Under the present accounting system, or the system heretofore in existence, you couldn't get that kind of information because the accounting system was geared to how many pencils they bought...in the performance budget, that [pencils cost] becomes the secondary classification - we still get that information (amount spent on pencils, etc.) but it becomes secondary, (primary is cost of carrying out individual functions).⁴⁰

In any event, with people in all walks of life, every where asking where their tax dollars were going and what they were getting for those dollars,⁴¹ the stage seemed ready for the performance budget. People had to have government expenditures explained to them in terms of individual work programs which would let them see at least several things:

- (1) The activity or function being supplied or carried out.
- (2) The unit (if possible) of measure by which the service was being supplied.
- (3) The cost per unit.
- (4) The total cost.
- (5) A strong indication that optimum efficiency was always being sought and that there was no wastage.⁴²

⁴⁰U. S. Congress, House, Committee on Expenditures in the Executive Departments, Budgeting and Accounting Procedures Act of 1950. Hearing before the Committee on H. R. 9038, July 11, 1950, 81st Congress, 2nd Session, (Washington, D. C.: Government Printing Office, 1950), p. 49.

⁴¹Municipal Research Bureau of Utica, N. Y., op. cit.

⁴²Ibid.

Because of the broad scope of this paper, it must suffice to state very briefly how we came legally to have a performance budget; we have seen the trend of thought gathering momentum toward the performance presentation, but legally the performance budget "arrived" as follows:

- (1) The Budget and Accounting Act of 1921⁴³ has been cited as implicitly embracing the performance type budget.⁴⁴
- (2) The performance budget was first given specific statutory recognition in the National Security Act Amendments of 1949; Section 11 of this Act prescribed a performance type budget in the military departments.⁴⁵
- (3) Additional support was given the performance type budget in the Budgeting and Accounting Procedures Act of 1950.⁴⁶ This Act provided for accounting changes and inclusion of statistical information upon which the performance budget depends.

⁴³42, Statutes at Large, 20.

⁴⁴U. S. Congress, Senate, Committee on Expenditures in the Executive Departments, To Improve Budgeting, Accounting and Auditing Methods of the Federal Government, Hearings before the Committee on S. 2054 and Amendments, Feb. 27, 28 and Mar. 2, 3, 6, & 7, 1950, 81st Congress, 2nd Session, op. cit.

⁴⁵63 Statutes at Large, 578.

⁴⁶64 Statutes at Large, 832.

CHAPTER IV

WHAT THE PERFORMANCE BUDGET IS

With the arrival of a performance budget, there was probably some conjecture as to "just what is a performance type budget?" and as a corollary, "how do we get on a performance type budget?" We shall examine each area in turn.

A good first approximation of a reply to "What is a performance type budget," was contained in a Department of Defense publication, undated, which as a matter of interest used a number of examples pertaining to the U. S. Navy. According to this publication:

A performance type budget divides the cost of a government department or agency into:

(1) Capital Costs, and

(2) Operating Costs. Previous budgets made no such distinction on a regular basis .

A performance type budget classifies operating costs as follows:

(a) For purposes of top-management control by:

(3) Identifiable programs and component functions, and

(4) Common supporting functions or groups of functions not identifiable with single specific programs. And,

(b) Also, for administrative cost control within agencies:

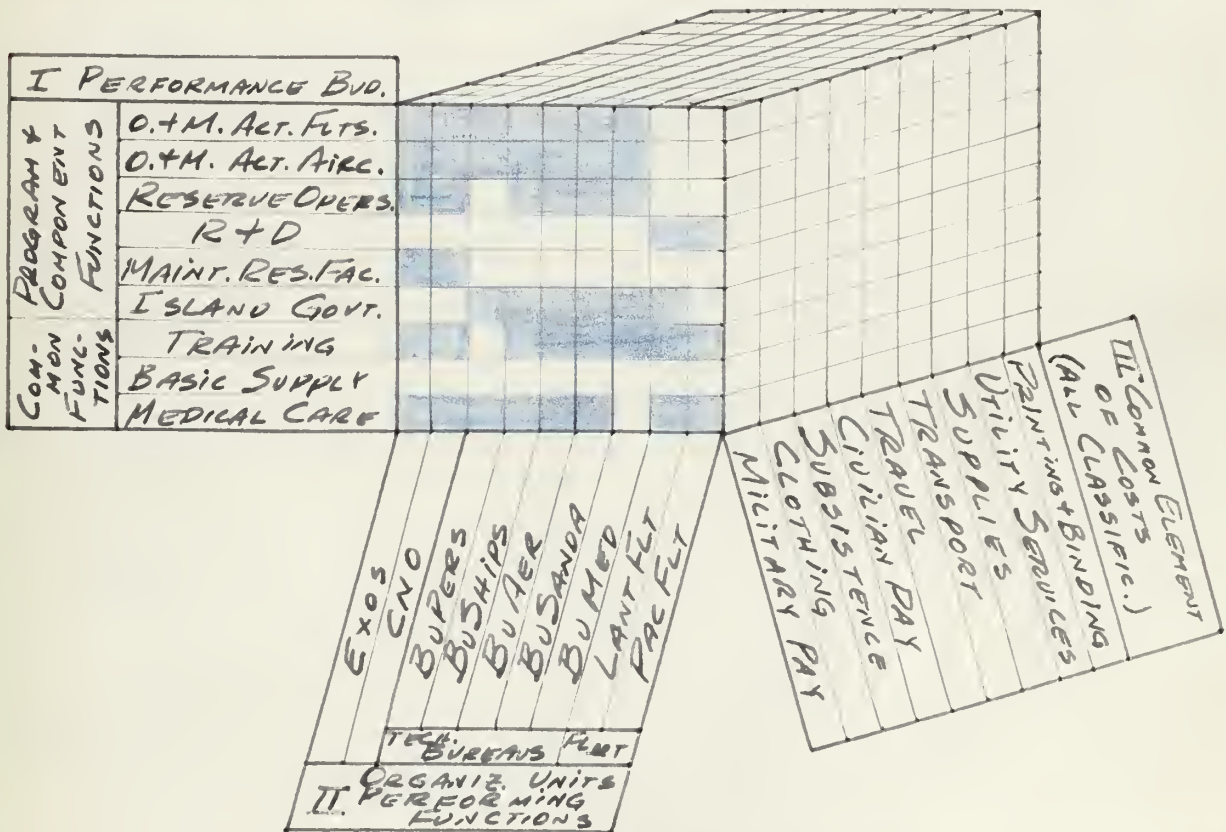
(5) By organizational units, and,

(6) By common elements of cost.⁴⁷

These classifications of operating expenditures for purposes of budgeting and accounting (based upon a Navy example), are succinctly illustrated by figure 1. Note that a classmates's comment on the performance budget as being merely "another way to slice up the cheese", appears pretty apt, in terms of this figure!

FIGURE 1

THREE DIVISIONS OF CLASSIFICATIONS OF OPERATING EXPENDITURES



(Based upon a Navy example)⁴⁸

⁴⁷ U. S. Department of Defense, What is a Performance Type Budget?, Prepared in the Office of the Secretary of Defense, (Washington, D. C., ca., 1949), pp. 1-22.

⁴⁸ Ibid.

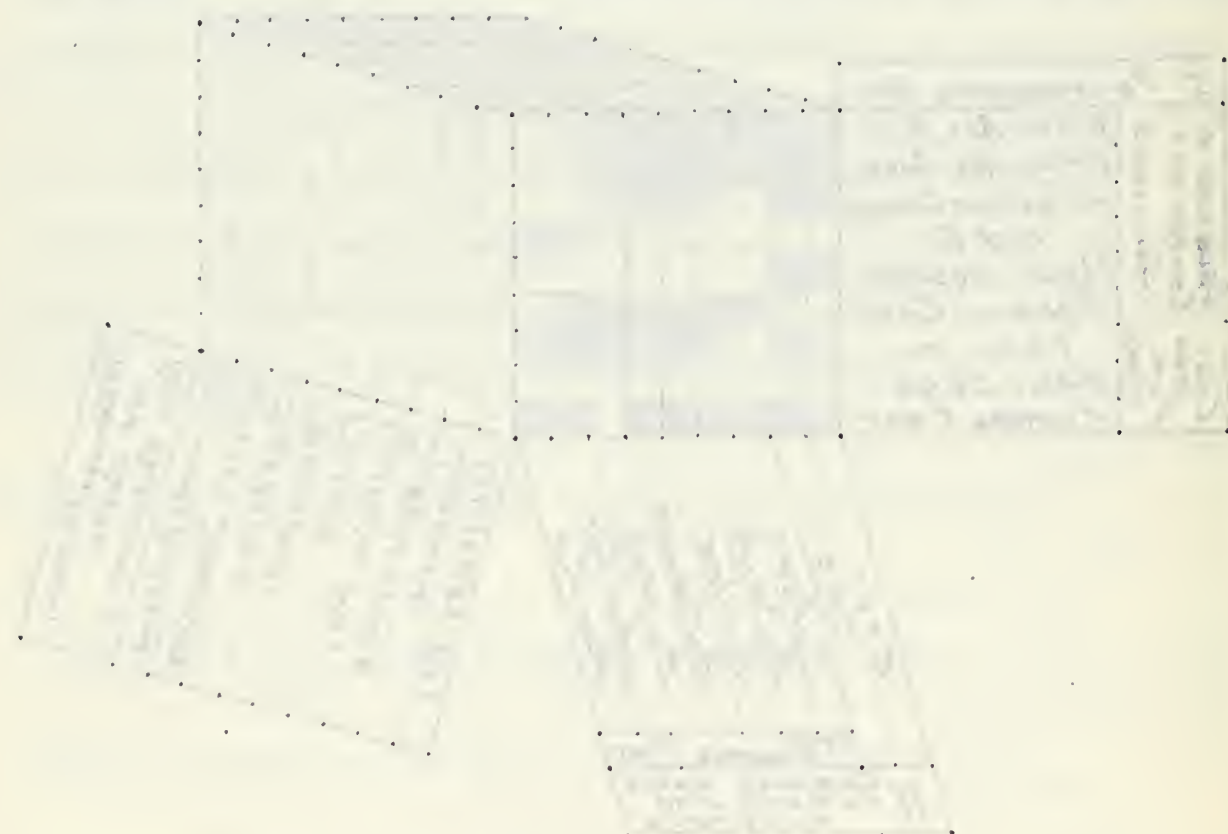
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The above publication held that the following were advantages for the performance type budget:

(1) Provides data on estimated annual costs of [attainment] of programs in terms of objectives, in order that top management may weigh the wisdom of relative amounts to be expended, and,

(2) Provides a simplified accounting system for control over costs of programs and operating functions, with administrative assignment of performance cost to, and reporting upon cost of performance by organization units responsible, and,

(3) Facilitates review by authorities.

We do not have either of the first two under the object expenditure type of budget.⁴⁹ The third area is now difficult.

As I review the advantages above, the advent of the performance type budget looks more and more like a parallel movement to the comptrollership growth we have seen in the last 50 years. As comptrollers have been installed to insure that top management has all the facts and data needed to successfully operate the large business, so similarly do the above-listed advantages of the performance budget enable top management to better comprehend the operation (in this case) of a military establishment. John F. Wilmott said, "A budget is a psychological device. Its primary purpose is to make people think."⁵⁰ I submit that when an organization is "large", that the performance budget alone will allow a person to think.

Another excellent explanation on what a performance type

⁴⁹Ibid.

⁵⁰John F. Wilmott, "Work Programs and Municipal Budgets," Public Management, Sept. 1945.

budget is, is contained in a U. S. Treasury Department publication on a related subject, entitled, Performance Reporting.⁵¹ Selected excerpts from this publication follow:

The Federal government recently made a fundamental change in the basis of its budget by adopting the concept of a performance budget.The President, with the Congressional Committee on Appropriations, has, [required] that budgetary estimates hereafter be prepared upon this basis.

The potential advantages of the performance budget cannot be realized until changes are made in the reporting and accounting systems which provide the data that go into the budget.

The bureaus of the Treasury... will proceed with the development of [required] revised systems.

The necessary revisions will be handled by each bureau's specialists.This pamphlet tells something about...the opportunities that the revised systems offer to management at all levels.

Section I: What the Performance Budget Is

Before the advent of the performance budget, Federal agencies presented their [expenditure estimates] in terms of "objects of expenditure", which represented a type of service or material to be paid for...example:

OBJECTS OF EXPENDITURE

01 Personal Services	\$1,622,500
02 Travel	144,500
03 Transportation of Things	13,000
04 Common Services	29,700
05 Rents and Utilities	9,100
06 Printing and Reproductions	8,000
07 Other Contracted Services	42,300
08 Supplies and Materials	48,000
09 Equipment	\$ 8,900
Total	\$1,926,000

This "object" classification was useful for analysis... but [failed to "price" the function being performed] and did

⁵¹U. S. Treasury Department, Performance Reporting, (Washington, D.C., U. S. Treasury Department: May, 1950), pp.1-21.

not reveal to reviewing authorities what would be accomplished if the budget were approved.

Bureaus talked about their "programs" at budget hearings...but the object classifications tended to draw attention away from the program presentation and toward the administrative details of personnel, travel, supplies, etc....the object classification method requested amounts based upon programs, but [never priced the programs]...it lumped all [costs] together and stated the cost in terms of the object categories. Thus, the programs were almost impossible to identify, analyze and to review.The performance budget reduces the object schedule to a supporting role and puts emphasis [instead] where it belongs, on the programs for which money is being requested.

The performance budget is based upon the bureaus "activities", that is, upon the things which the bureau proposes to do. It thus focuses attention upon basic questions of public policy - the desirability, size and cost of the proposed programs rather than the administrative details. The expenditure estimates set forth above, are [re-cast below in performance budget format]:

ACTIVITIES

Suppression of counterfeiting and	
investigation of forgery	\$1,434,166
Protection of President of the U. S.	337,134
General Administrative Expenses	116,687
Executive Direction	<u>38,013</u>
Total	\$1,926,000

[It is evident] that this type of presentation is much more meaningful since it clearly shows what the organization, in this case the Secret Service, proposes to do with the money it is asking for. [The added meaningfulness] provides a sounder basis for the formation of the estimates, for their analysis, and for execution of the budget plan.

The activity statement shows only the broad outlines of the proposed program. It would, of course, have to be supported by supplementary statements showing in detail the operations included in the activity, and the method of computing costs.⁵²

After these two descriptions of what a performance budget

⁵²Ibid.

is, it is probably relevant here to pause and note that the "Cost" of a performance budget, at first appears to be:

- (1) Most "old" data (object classifications) will remain - as supporting or secondary data.
- (2) The "new" activity statements will be supported by statements showing in detail the operations and pricing methods.

Although I advocate the performance budget, it is a service that costs something - I merely feel the costs are far outweighed by the advantages.

The above Treasury Publication goes on to Performance Reporting:

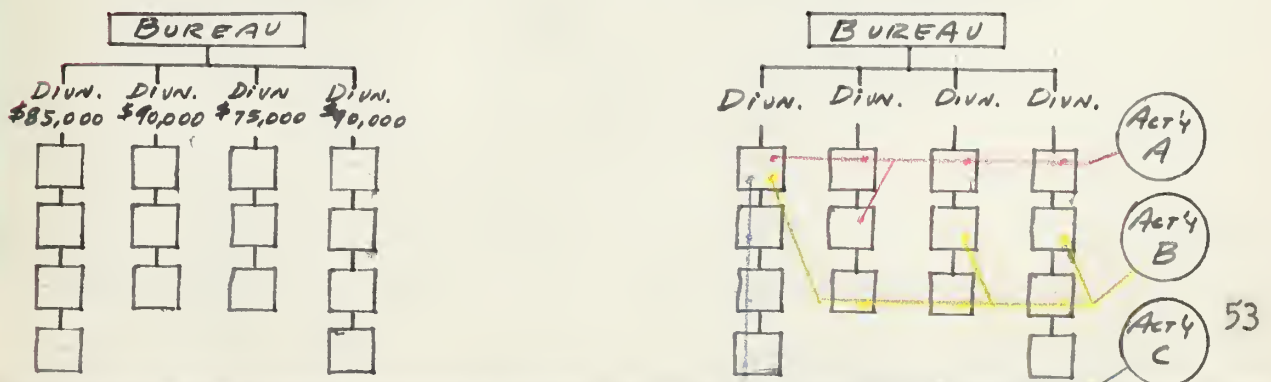
Section II - What Performance Reporting Is

If a bureau is going to base its budget on its activities, it [needs] financial and operating reports on each activity so that it can show for each of them their workload and accomplishments on the one hand and costs [with] related financial data on the other. Performance reporting systems therefore are based on the activities used in the bureau.

In most bureaus, reporting and accounting systems are based on organizational structure, as is shown in Figure 2. below.

FIGURE 2

PERFORMANCE REPORTING IS BASED ON ACTIVITIES



Such reporting will provide activity data only if activities coincide exactly with organizational structure as in the case of Activity "C" in the above figure. If activities cut across organizational lines, as do Activities "A" and "B", it will be necessary to change the reporting and accounting systems so that they will present the necessary information on activities. Thus, the first thing that a bureau has to do is to identify its major functions, divide these functions into activities, and establish such further sub-divisions of the activities as are desired for budgetary and management purposes. This will provide the framework on which budgetary, accounting and reporting systems should be based. Ideally, this framework should be related to the organizational structure in such a way as to facilitate the decentralization of operations, budgeting, program and financial responsibility to every level of management.⁵⁴

At this time, earlier advantages claimed for the performance budget by the Navy Department in conjunction with its alternate form of budget submitted for fiscal year 1948 and already quoted herein, are more understandable:

(1) Fiscal Management Would Parallel Management Responsibility⁵⁵

Consider herein the above Figure. Notice that as existing, the person in charge of seeing that Activity "A" and Activity "B" are properly prosecuted, must be the single individual at the head of the bureau. If we use the performance type budget and reporting systems and appoint an officer in charge of Activity "A" and one in charge of Activity "B" (with budget and necessary authority), the bureau head can devote his time to bureau - planning rather than "putting out fires" in two subordinate activities - his activity Officers do that.

⁵⁴ Ibid.

⁵⁵ Department of the Navy, Proposed Revision of the Naval Appropriation Act, Nav Exos 13048, op. cit.

(2) Internal Management Would be Less Complex⁵⁶ Here again we see the activity Officers concerned only with that over which they respectively have financial and management responsibility.

(3) Fiscal Control Would be Facilitated⁵⁷ Here we see that all expenditures for each activity are clearly made under allotments for those respective activities, and top management receives the fiscal information necessary for comparison and control.

(4) Budget Presentations Would be More Effective⁵⁸ Here each bureau would present complete estimates for its own activities and would present their needs in terms of their work programs.

A further examination is now in order to see what an activity schedule is, especially in view of the extensive use of that expression in the Treasury Publication quoted above. Such a review is contained in a Bureau of the Budget publication which actually predated the above quoted Treasury Publication. The Budget Publication goes on to say:

An activity schedule is an arrangement of financial data which portrays the purposes served or the programs carried on under an appropriation or fund and is the structure of the Program and Performance section to be printed in the budget document. [Activity may well be merely the funds for doing something].

The structure of the Program and Performance section to be printed in the budget document must:

- (1) Consider the major purposes,
- (2) Determine programs carrying out these purposes,
- (3) Express program activities carried out under each appropriation or fund.

⁵⁶Ibid. ⁵⁷Ibid. ⁵⁸Ibid.

Program activities should be expressed in terms of programs or objectives and not in terms of organization.

The most informative method of expression may be according to:

Projects - Such as "Alterations to Medical Building".

Subject Matter or Product - Such as "Maintenance Cold Storage Plant".

Recipient or Clientele - Such as "Old Age Assistance."

Location or Institution - Such as "Rio Grande Canalization".

Combination of above.⁵⁹

Returning to the U. S. Treasury Publication quoted above:

After the activity pattern has been established, the next problem is to devise [a work measurement system] [by which] each activity can show in specific terms what it intends to accomplish with the funds asked for, and what it accomplished with funds previously appropriated.

The key to such measurement is the selection of a "work unit" which is some product or aspect of the work that can be counted or measured...examples of such work units are: tax returns processed, checks issued, guard posts manned, forgeries investigated, actions taken, cases closed.

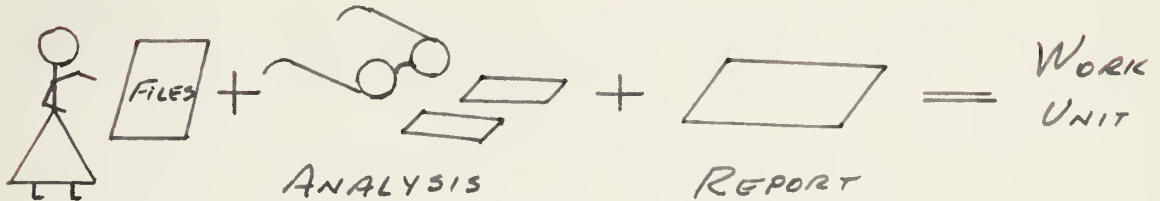
The work process illustrated below shows the steps in an activity which involves the conduct of certain investigations, such as searching files, analyzing, and finally reporting. The report submitted contains the findings and could be the work unit if an overall measurement for the whole process is desired. If more detailed measurement were required, a work unit could be established for each step in the work process, such as "number of files pulled", "the number of analyses completed", etc.

Since this work process is not uniform, the measurement may be rather rough. Some of the reports would represent more work than others, yet useful average figures will be obtained. If differentiation were required, reports could be classified further as to difficulty.

⁵⁹U. S. Bureau of the Budget, Improving and Extending Activity Schedules, (Washington, D. C., U. S. Bureau of the Budget: 1949), pp. 1-18.

For Each Activity

The Performance Budget Shows Work Accomplished:

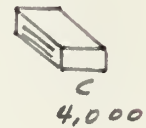


Reports may show:

- (1) Volume of work load
- (2) Volume and time of workload
- (3) Volume, Time and Costs

(1)

VOLUME



(2)

TIME

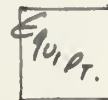
A
7,200
33,000 M-H
4.6 M-H Ea.

B
9,100
20,000 M-H
2.5 M-H Ea.

C
4,000
13,000 M-H
3.3 M-H Ea.

(3)

COST



\$100,000

\$4,000

\$300

\$1,150

(A) \$50,000 + \$2,000 + \$300 + \$1,050 = \$53,350
D 7,200

(B) 30,000 1,500 300 50 = \$7.40

(C) 20,000 500 300 50 PER UNIT

Mathematical Induction

The following table shows the results of the induction process.



Let $P(n)$ be the statement that

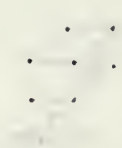
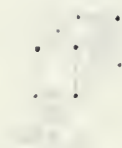
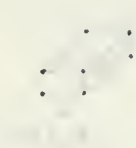
$1 + 2 + \dots + n = \frac{n(n+1)}{2}$

is true for all $n \geq 1$.

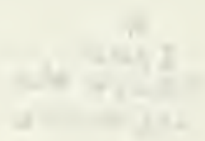
We will prove $P(n)$ by induction on n .

Base Case:

(1)

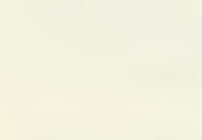


(2)



Inductive Step:

(3)



(4)

(5)

(6)

Systems based on (1) above (Volume of workload) require only the selection of a satisfactory work unit; thereafter recording and reporting are quite simple...A [refinement] is to include also man hours (2) above, (inasmuch as time on the job is shown, which factor is affected by working days in the month, sick days, etc. which are not revealed by (1) above). When man-hours are included, we are on the way to determining unit costs. And (3) above facilitates true performance type presentation.⁶⁰

Inasmuch as selection of the work unit is rather basic to the performance type presentation, attention thereto is merited at this point, especially in view of the usual unfavorable reception I have noted for work-measurement programs and the dilemma noted in contemporaries (and myself) in definition and selection of a work unit. Selection of a meaningful work unit has been reported informally as having aided at least one bureau in gaining the confidence of questioners at congressional hearings.⁶¹

Although the performance type budget has given rise to a volume of literature, there is a dearth of information on the "how to" of getting on the performance type budget. Although one of the bases of the performance type budget is selection of a work unit, a dilemma has been caused in this area because, although some work is readily measurable or countable, work units must be "invented" for other areas of work. In fact it has been said, "That as our tools of measurement sharpen, the line between

⁶⁰U. S. Treasury Department, Performance Reporting, op.cit.

⁶¹Statement of Supply Corps Officer, U. S. Navy, In Navy Comptrollership P. G. Group, George Washington University, Writer's Class Notes, (Washington, D. C.: 1954).

measurable and non-measurable areas will change."⁶² One approach to measurement in the measurable areas is the Man-Hour Approach. This consists in its simplest form of arriving at the total number of work units estimated for the budget year, and deriving the number of man hours required for that year by recourse to the man-hour per work unit ratio of previous years. An advantage of this system is that it is simple. By using this simple system, the City of Los Angeles was able to get on the performance budget in most City Departments in one year.⁶³ However, the man-hour approach is not useable in certain non-measurable areas. An example given concerning a municipality is "...a City Fire Department in which the number of fires extinguished provides no basis on which to budget."⁶⁴

Two systems have been used **successfully** in the non-measurable area; they are:

- (1) Ratio of Personnel basis and
- (2) Point Grading System.⁶⁵

The Ratio of Personnel basis relates the number of personnel required to a definite organization index. Most commonly, such ratios have been used to determine service and staff needs. For instance, in the Federal Government, one personnel employee is allowed to every 110 civilian employees and one payroll employee

⁶²Frank Sherwood, "Some Non-Cost Accounting Approaches to Performance Budgeting", Public Management, Vol. XXVI, Jan. 1954, p. 9.

⁶³Ibid. p. 10. ⁶⁴Ibid. ⁶⁵Ibid. P. 11.

doing payroll, leave and retirement accounting is allowed to every 235 civilian employees. In other cases, a flat percentage figure is used, as in the case of Standard Oil of New Jersey which specifies that a total of 15% of personnel may be supervisory.⁶⁶ Citing specifically from the work of Frank Sherwood on Some Non-Cost Accounting Approaches to Performance Budgeting:

In the case of a municipal fire department with a well-established table of organization, the number of companies necessary to provide a certain level of service is determined by intensive administrative research. Having figured the companies needed, the total personnel complement can be derived by reference to previously developed manning tables. In the city of this example, area manning standards were:

Pumper Company	4 Men
Extension Ladder Co.	6 Men
Pumper and Ladder Co.	5 Men

Further data for this area were:

- Average Salary, \$4,500 per man
- 67 hour work week
- 1 Man to every 19.3 regular men required for vacations
- 1 Man to every 70 regular men required for sick leave
- 1 Man to every 4 regular men for relief and day off

When it was determined that a department consisting of 19 pumper companies, two extension ladder companies and 4 Pumper and Ladder Companies was required, the budget estimates fall quickly into shape as follows:

(a) Regular Personnel Total, 137 . . .	\$616,500
(b) Extra for vacation 7.1 men . . .	31,950
(c) Extra for Sick Time 2 men . . .	9,000
(d) Extra for days off, 34.2 men . . .	<u>154,000</u>
Total . . .	\$811,450 ⁶⁷

At this time, I must question what would happen, if, after

⁶⁶Ibid. ⁶⁷Ibid.

deciding the size of a department, it was found that the total cost was more than the municipality could bear, what would happen? I presume a preliminary study had shown that a total, in the above case, of about \$811,450.00 was what the municipality could in fact stand. I must note also, that we are accepting as "gospel", so to speak, certain personnel ratios that affect the total cost. I presume that in this case we do accept them because this town was stated to have well-established manning tables. With continued performance budgeting, as I see it, the well established manning tables will in fact become well-established by repeated critical comparison with various other standards.

To return to our systems, we next consider the point grading system. This consists in simplest form of establishing, through rigorous study and attention to detail, a "Model" organization. An example given has been a city recreation center.⁶⁸ At least four variables exist in any activity within a city recreation department in discussing the size of a center and its staffing, they are:

- (1) Size and Facilities
- (2) Population Served
- (3) Record of Usage
- (4) Hours Open

Having established standards and staffing for the model, all other centers in the same department are then graded in

⁶⁸ Ibid., P. 12.

relationship to the model, based on above listed variables. The grade then governs personnel assigned. Although this system can be time-consuming to set-up, it has merit as evidenced in the City of San Diego, where the grade point system was installed in its recreation department "...at a cost of \$1,800.00 in staff time; and in the first year, savings [attributable to the system] amounted to \$25,000.00."⁶⁹

Establishing a measurable work unit may well cause more of a dilemma than it should, to a prospective user of the performance budget. Measuring office work, for instance, is somewhat new, and it has been my observation (with limited experience), that such measurement stirs up psychological "brick walls". People think they don't want to be measured and checked upon, and of course it has been said that what a person thinks is a "fact" to that person. Probably the name generally applied to such work unit counting is the major reason for the unpopular reception given "Work Measurement" as it is called. Standard Oil Company of Ohio has a much more "polite" name for the same thing, i. e. "Socony Work Analysis Program", usually referred to by the innocuous short title of "SWAP".⁷⁰ In that company, the system was reportedly ... "going over well",⁷¹ and I attribute it in some measure to the psychologically sound

⁶⁹Ibid.

⁷⁰Statement of Officer of Standard Oil Company of Ohio, before Navy Comptrollership P. G. Group, George Washington Univ., Writer's Class Notes, (Washington, D. C.: 1954).

⁷¹Ibid.

move of not using the term work measurement to describe it. The dilemma about choice of a unit of work measurement is a real thing--consider the following statement made as late as 1954, before a work shop of the Municipal Finance Officers Association of the United States of America, considering the performance budget, "...of course there are many operations that cannot be measured, such as street patching, stormwork and sidewalk defects".⁷² (Underscoring mine). Contrast this with the quarterly Budget Report of the Village of Wayne, Michigan already quoted herein, where they had measured street patching.⁷³

As I studied work measurement, I drew the conclusion that a bureau is considered to have made an important stride, if it has been able to define a unit of work measurement, and to apply it. The most important gain lies in being able to compare current figures with own activity for other periods, and to compare with other comparable activities. To me the lesser gain, but a major gain to many individuals, is the gain achieved when that bureau can "point with pride" to its work measurement system, as it substantiates its expenditure estimates before all reviewing authorities. I hope that the present emphasis on work measurement so that "we can merely use it to get funds," doesn't get to be a "bandwagon" of "fast" slide-rule and calculator operators. I hope

⁷²Municipal Finance Officers Association of the United States and Canada, "Administrative Uses of Performance Budgets", discussions during two 1954 workshop sessions, Accounting Publication Series, No. 11-3, (Chicago, Illinois: 1954) p. 9.

⁷³Village of Wayne, Michigan, Quarterly Budget Report for Quarter Ending Sept. 30, 1948, op. cit.

that instead, work measurement, in conjunction with our performance budget, is used as a tool for me to improve my activity, and not as a "gimmick" for me to oversell my expenditure estimates.

My conjectures on work measurement have continually been influenced by my background in the only thing I know anything about, the U. S. Navy. To my mind, our Navy is much like a municipal fire department (or any other emergency department, but in this discussion I shall say fire department because we have above cited "non-cost Accounting Approaches to Performance Budgeting" in a municipal fire department).⁷⁴ Hence we must be careful when we hear others say, "However, some emergency services must be budgeted on a stand-by rather than on a unit-production basis - a notable example is the city fire department."⁷⁵ The implication here is that we cannot methodically gauge our work. This is not so as brought out in the foregoing discussions. It behooves us in the Navy to measure or gauge everything we do, in one way or another, to realize both advantages shown above, i.e. - (1) For valid comparisons to the end of a better organization, and (2) Justification of expenditure estimates.

Having now proceeded through measurement of work units and "costing" an activity, we may view the estimate of expenditures under a performance budget according to Figure below:

⁷⁴Frank Sherwood, "Some Non-Cost Accounting Approaches to Performance Budgeting", Public Management, op. cit., p. 12.

⁷⁵Contra Costa County Taxpayer's Association, An Approach to the Technique of Performance Budgeting, op. cit., p. 2.

BUREAU

- ADMIN. DIV.
 - \$5,000
- SERVICES DIV.
 - \$6,000
- PROD. UNIT #1
 - \$4,000
- PROD. UNIT #2
 - \$7,000
- PROD. UNIT #3
 - \$3,000
 - 01
 - 04
 - 08

BY ACTIVITIES

- ACT'Y. A \$30,000
- ACT'Y. B \$10,000
- ACT'Y. C \$12,000

BY OBJECTS

- \$2,000
- \$2,500
- \$5,500
- \$7,000

BY ORGANIZATION

- \$10,000
- \$10,500
- \$9,500
- \$14,000
- \$8,000

THESE ARE THE RESULTS OF THE ANALYSIS OF THE DATA OBTAINED FROM THE EXPERIMENT. THE RESULTS ARE GIVEN IN THE TABLES AND FIGURES. THE RESULTS ARE IN GOOD AGREEMENT WITH THE THEORY.

TABLE I

MEASUREMENTS OF THE DIFFERENTIAL CROSS SECTION



THE RESULTS OF THE ANALYSIS OF THE DATA OBTAINED FROM THE EXPERIMENT ARE GIVEN IN THE TABLES AND FIGURES.

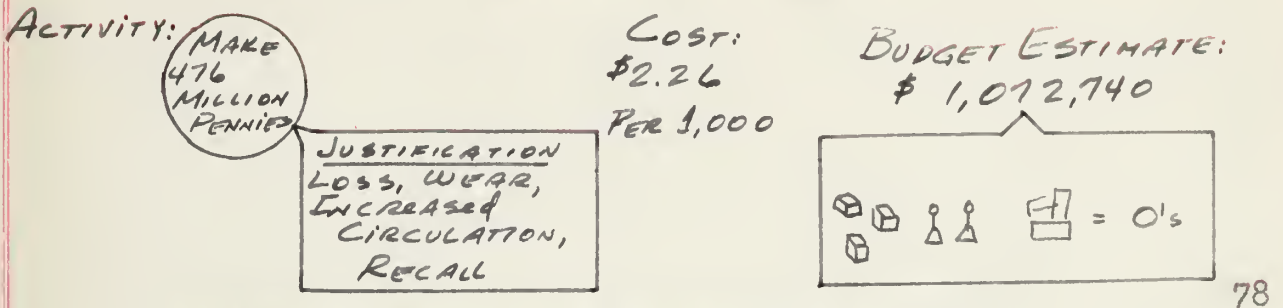
Here we see that the Bureau is carrying on three activities; all divisions contribute to Activity "A", while the work of Activity "B" and "C" is performed mainly in production units #1 and #2, respectively, with some support from the Administrative and Service Divisions. In addition to costs tallied according to object classification and by divisions as usual, we see the activity costs also. These activity costs are the pulse that the Officer in charge of each activity guards constantly. Observation shows that some added reporting has been inserted to give us our performance type budget, but, it has been held, and I agree, that good managers probably already use the data which has now been "officially" added to the reports required; we have merely cleared the air by setting things down on paper.⁷⁷

In actual budgeting (estimating, justification and execution), the performance budget is a workable and businesslike tool of management. When only the object classification type budget is used, management concerns itself mainly with "administration," and budgeting is taken care of in some side office. When the performance budget is used and management at all levels is given its task from the same hand that dispenses funds to accomplish the task with, everything becomes businesslike and management becomes "cost-conscious". Budget expenditure estimates are derived as simply, basically, as Figure 4 below indicates:

⁷⁷Ibid.

FIGURE 4

BETTER BUDGET FORMULATION



Basically, expenditure estimation is simply:

- (1) Estimation of scope of activity for budget year together with reasons therefore.
- (2) Derivation of total cost based upon previously recorded costs.

Presentation of the expenditure estimates for review is again basically as simple. The Bureau merely outlines what it will do if it receives the funds asked for, and tells what it accomplished with funds previously allocated. It is thus clear to the reviewing authorities, what they will get for the monies finally appropriated.⁷⁹

Another great advantage of performance budgeting accrues in "Performance Reporting", because the data, and dollar amounts used in the budget are also used by operating management. These budget figures, when compared with periodic expenditure reports, reveal the accomplishments of each program and keeps management on "top" of the job. By relating current figures with figures of other comparable activities and with comparable own figures for

⁷⁸Ibid., p. 17.

⁷⁹Ibid.

other periods, program analyses are made possible. Performance Reporting, as these periodic "budgeted and actual" figures are called, also accumulates valid work load data, and enables forecasting. It has been held, that performance reporting increases interest of all hands, up and down the line, by informing all concerned where they are, where they are going, and what the plans are for getting there.⁸⁰ This sounds to me pretty much like the comptroller's function, except that the comptroller, using the same data, merely makes his report to top management who in turn notifies all concerned.

Development of Performance Reporting has been succinctly set down as follows:

(1) Development of an overall activity classification and of the breakdowns desired for budgeting, accounting and reporting purposes.

(2) Selection of meaningful work units for each activity.

(3) Revision of fiscal and account procedures to better reflect activity costs.

(4) Realignment of reporting system so that it will provide performance data on an activity basis.⁸¹

Apropos of what management does with these newly reported data (Performance Reports), is the following:

Budget control, no matter how complete in terms of forms and systems, must have roots in an effective management program for evaluating performance and increasing the efficiency of operations.

The fundamental factors determining [government] costs are the variability of activities and the standard of services to

⁸⁰Ibid. ⁸¹Ibid.

be provided. Existing practices, whether good or bad, ought not to be taken for granted, but should be critically reviewed by the chief administrator and his department heads. Comparison of service levels with those of other cities and with recommended "model" standards may be helpful.⁸²

Or to summarize, "The performance budget will be an essential management tool for city administrators in developing standards of municipal service."⁸³

Thus we have seen a:

Trend toward considering municipal governments as production operations rendering definite services, many of which can be measured in terms of production units. Other services, while not entirely subject to work volume measurements, can be analyzed in such a way that budget requirements and cost control systems can be based on factual criteria.⁸⁴

At this time it should be noted that, "San Diego considers its performance budget as a contract between the public works department and the city manager,"⁸⁵ for "priced" services to be rendered, I must add.

It has further been held, that because of the "cost-conscious" atmosphere of the performance budget, "It is a medium by which actual field activity can be brought to the budget examining committee in understandable terms."⁸⁶ It also, "...provides

⁸²S. M. Roberts, "Management Analysis and Evaluation", Public Management, XXXIV (Dec., 1949), 314-317.

⁸³S. M. Roberts, "Trend Toward Performance Budgeting", Public Management, XXXIV (Oct., 1952) 223-226.

⁸⁴Ibid.

⁸⁵Municipal Finance Officers Association of the United States and Canada, "Administrative Uses of Performance Budgets," op. cit. p. 13.

⁸⁶Municipal Finance Officers Association of the United

a [mechanism] by which ultimate organizational and procedural changes may be instituted for greatest efficiency."⁸⁷

States and Canada, "Performance Budgeting for Libraries", the analysis and measurement of budgetary requirements for the operation of Library services, Accounting Publication Series No. 11-4, (Chicago, Illinois: 1954), p. 9.

⁸⁷Ibid.

CHAPTER V

FEDERAL GOVERNMENT SHIFTS TO THE PERFORMANCE BUDGET

In the fall of 1949, the Department of the Navy set forth its "Principles followed in arriving at a program Budget Structure on a Performance Basis." Quoting from the publication of that name:

1. The primary objective of a performance budget is to provide top management (reviewing levels such as the Sec. Nav, JCS, Sec Def, Bu Bud, and Appropriations Committees of the Congress), with information for purposes of considerations and control on the basis of PROGRAMS, representing plans of action to accomplish an objective or mission, as well as areas of particular interest or significance.

2. To provide for the balanced support of programs, the funds for a particular program must be in a single appropriation. The paralleling of fund and management responsibility would consequently be accomplished by the Secretary through the allocation process as well as the appropriation process.

3. Since many Naval functions are establishment-wide, the Navy has two types of programs - those which are of a Primary nature such as "Aircraft and Facilities", and those which are service-wide, such as, "Service-Wide Administration and Operations." Since it would not be practicable to distribute service-wide functions to primary functions, the undistributed portion should be appropriated for separately.

4. The funds for primary programs should be as inclusive as possible. For example, in maintaining and operating an air station under "Aircraft and Facilities", funds for all types of work directly related to this program should be included, such as supply departments, fiscal work, maintenance of ordnance for aircraft, and other items of this nature which may be presently appropriated for separately.

5. Insofar as consistent with the above principles, items included in an appropriation should be readily adaptable to inclusion within a single major heading under the National Military Establishment cost categories in order to avoid situations where funds must be spread through various categories.

6. In certain instances where the line of demarcation between programs is not clear-cut, the following guide lines should be followed:

(A) Functions which could logically fall into either of two programs, should be assigned on the basis of dominant interest and the greatest feasibility from an appropriation, management, budgetary, and accounting viewpoint. (Example "Hospital Slips - "Medical and Dental Care" or "Ships and Facilities").

(B) Where two or more programs are being carried out on adjoining property, or where one is tenant of another, costs should be borne by each as follows:

(1) Contributing services should be allocated among programs insofar as practicable.

(2) Where allocation is impracticable, cost of contributing services should be borne entirely by the major consumer, or furnished by the contributing service itself from a Service-Wide appropriation.

(C) Contributing services which exist mainly to support a primary or service wide program, should be included as a part of the cost of such program. (Example- Fiscal office of an air station may serve other local activities, but its primary reason for existence is to serve the air station).⁸⁸

This was the philosophy in the Department of the Navy on the eve of its first program budget presentation, since the "alternate form" had been submitted in 1947 in addition to the conventional form. The guide lines set forth above look workable enough to me to facilitate decision making down to the field on

⁸⁸Department of the Navy (Office of Budget and Reports), "Principles Followed in Arriving at a Program Budget Structure on a Performance Basis," (Washington, D. C., Navy Department: Nov. 18, 1949).

matters of where to place charges (in this case estimates of expenditure). Undoubtedly the experience with the 1947 Submission in "alternative form" (for fiscal year 1948), facilitated submission of the fiscal year 1951 estimates. Departments that submitted for fiscal year 1951 in complete program format were:

Department of the Interior
 Department of Justice
 Post Office Department
 Department of the Navy, and
 General Services Administration

Some other departments submitted at that time without complete use of program format.⁸⁹

After submission of the Presidents' Budget to Congress, the Department of the Navy published a booklet entitled, Concept of the Navy's 1951 Performance Budget. This booklet re-iterated information quoted above from n. 88, and added that "...a further consideration in determining programs, was that programs [where possible] should lend themselves to comparison with the Air Force and Army."⁹⁰

In early 1950, Mr. Herbert Hoover hailed the President's Budget submitted on January 9, 1950, as the "...greatest advance

⁸⁹U. S. Bureau of the Budget. The Budget of the United States Government for the Fiscal Year ending June 20, 1951, (Washington, D. C., Government Printing Office, 1950), p. 3.

⁹⁰U. S. Department of the Navy, "Concept of the Navy's 1951 Performance Budget", (Washington, D. C., U. S. Navy, Office of Budget and Reports: 1950), p. 21.

in budgeting since 1920".⁹¹ Presumably the trend and legislation already on record were interpreted to mean that the old object classification type of budget, would soon completely disappear, except as those data appeared in a supporting role.

In still early 1950, Mr. Robert L. L. McCormick, Research Director of the Citizens Committee for the Hoover Report, said, "...the advance [achieved by going to the performance type budget] will fail unless accounting in the Federal Government goes on apace."⁹² What Mr. McCormick was saying of course, was that mere presentation in performance style, which is not much of a trick of itself, will, of itself do little good. What is needed for true performance management, is a chart of accounts that will facilitate performance reporting (which has already been covered herein).

Even though we were well into performance budgeting in early 1950, an interesting, but to me illogical news release actually made in behalf of performance budgeting by the Citizens Committee for the Hoover Report, stated:

Under the earlier system [of budgeting] , the U. S. Navy could not say what it cost to operate the Brooklyn Naval Shipyard. But they knew the cost for "all personnel services" or "all supplies". If, under this older government system, in your household budget you would lump together under "personnel services" such items as plumbing repair jobs, baby sitting service and haircuts, there would be no way in which you could

⁹¹Citizens Committee for the Hoover Report, "The Future of Program Budgeting", a progress report by Robert L. L. McCormick, Research Director, (Washington, D. C., Citizens Committee for the Hoover Report: May 29, 1950), p.2.

⁹²Ibid.

tell how much you expected to spend for baby sitters or plumbing repairs. Likewise in your budget under "Supplies", you would not know the expected costs for food or gas, or writing paper, because they all would be lumped under "supplies".⁹³

This seems to me to be a pretty poorly reasoned out release about a budgeting change of great importance. It completely misses the point that a performance budget (to stay with the household example), would be a tool that would let me know pre-cisely what it cost to feed my family by properly placing charges for all food, gas for cooking, water for cooking, electric power for cooking and labor for cooking, in one activity account probably entitled "Feeding Family and Guests". Likewise, baby sitting fees would be placed in an account probably called "Recreation", and also properly placed in this account might be all charges for theatre tickets, parking car while at theatre, ski-lodge fees, admissions for family to Glen Echo Park, admissions to Uline Arena, et al. Either the advocates of the performance budget missed the point in the release quoted above, or I have missed it, and I don't think I missed it. My point here is, that even the experts can "miss" on just what the performance budget is.

As the fiscal year 1951 budget was going together in the several offices in Washington, Budget Director Frank Pace, Jr., stated that the budget "...would be presented on the performance basis,"⁹⁴ and that the change most noticed would be the addition

⁹³Citizens Committee for the Hoover Report, "Background Report on the Federal 'performance' budget," (Washington, D. C., Citizens Committee for the Hoover Report: 1950), p. 2.

⁹⁴U. S. Bureau of the Budget, "Announcement by Director

of textual statements of "program and performance",⁹⁵ rather than the usual "...tabulation of financial plan of year and language sheets."⁹⁶ He announced that another change would be "...improvement of "activities schedules" in that in the past, more than half the programs [of Federal Government] were [not "priced"]", but in the future over 90 percent of the appropriations would be to support a definite program, function, or activity."⁹⁷ Mr. Pace went on to say that "...missing will be long lists of civilian positions...the appropriations committees will be able to get from agencies, personnel data tailored to the committees needs...only summary figures for total employees and dollar totals will be shown in each appropriation."⁹⁸

When the fiscal year 1951 President's Budget was submitted to the Congress, the President said, in part:

The content and arrangement of this part of the budget have been changed this year to give greater emphasis to the work programs and "performance" on which the financial requirements are based. The objective of these changes is to make the budget a more complete and informative document with respect to the success to be performed by each agency and the money requirements for such services. Development in this direction will take several years to complete. A new pattern of appropriations is proposed [herein] for the Department of Interior, Department of Justice, the Post Office Department, the Department of the Navy, and the General Services Administration. Less complete changes in pattern are proposed for a few other agencies. The changes generally will bring together the appropriations for a program or group of related programs in each agency. Revisions for several other agencies are contemplated for the 1952 budget.⁹⁹

Frank Pace, Jr.", News Release, (Washington, D. C., U. S. Bureau of the Budget: Thursday a.m., August 4, 1949), pp. 1-2.

⁹⁵Ibid. ⁹⁶Ibid. ⁹⁷Ibid. ⁹⁸Ibid.

⁹⁹U. S. Bureau of the Budget, "The Budget of the United

It is interesting to note, that although the performance budget was in a strictest legal sense required only of the Department of Defense, that a number of other Federal Agencies, "made the boat" with performance type expenditure estimates. It is also interesting to note that the Navy Department which "owned" the over-worked "horrible example" of the "Naval Hospital Bethesda with its many appropriations", was the one department so specifically required by statute, which did make the deadline. The appearance of the General Services Administration, a "new" government agency, on the early list of performance budgeters, speaks well for that agency.

Now that we have traced the background and "arrival" of the performance budget, it may be interesting to make a very "broad brush" examination of some attributes of the Federal Budget for the budget years 1949 (well before performance budgeting) 1951 (the first appearance of Performance Budgeting), and 1955 (the performance budget with us for a period). This examination includes only the Department of the Navy, and is presented below in Table I.

A glance at Table I shows the relative amounts of "paperwork" included in the budgets for the several years. Mr. A. E. Buck, previously quoted herein, had been prompted toward a performance budget in some considerable degree because that budget was alleged to be shorter, would take less time, etc. It is

TABLE 1

EXAMINATION OF A SEGMENT OF THE FEDERAL BUDGET FOR SUCCESSIVE YEARS

Budget Year	Authority	Setting	One Area (Research, Navy)	Format for	Total Pages
FY 1949	a	No Performance Budgeting Personnel Details Included	<p>"For expenses", etc. - Language part for legislation purposes</p> <p>"Funds available for obligation"</p> <p>"Obligations by Activities" Note 1</p> <p>"Obligations by Objects"</p> <p>"Detail of Personnel Services"</p> <p>Note 1 - Activities used in sense of administrative entity, not function</p>		54-1/3
FY 1951	b	Start of Performance budget Personnel data supplied by Dep'ts to Congress	<p>"Funds Available for Obligation"</p> <p>"Program & Performance" - a textual explanation of what program does.</p> <p>Some performance data included such as "cost of engine overhauls", "line items", etc.</p> <p>"Obligations by Activities" (Note 1 above applies)</p> <p>"Obligations by Object"</p> <p>"Appropriation Text" (Language)</p>		46-1/4
FY 1955	c	Performance Budget with us for a period Appendix contains Personnel Data	<p>Essentially same as for FY '51 above except more performance data included, such as "Packing" in "Tons"; "Preservation" in "Units Preserved"; "Storage" in "line items".</p>		36, plus 39-1/2 in Appendix; Total 75-1/2

a U. S. Bureau of the Budget, "The Budget of the United States Government for the Fiscal Year Ending June 30, 1949," (Washington D.C., Government Printing Office: 1948).

b U. S. Bureau of the Budget, "The Budget of the United States Government for the Fiscal Year Ending June 30, 1951," (Washington, D. C., Government Printing Office: 1950).

c U. S. Bureau of the Budget, "The Budget of the United States Government for the Fiscal Year Ending June 30, 1955," (Washington, D. C., Government Printing Office: 1954).

therefore interesting to note that although personnel details slipped out of the budget in fiscal year 1951, it was back in greater force than ever in fiscal year 1955. I suppose the reason the details are back (albeit in Appendix), is that reviewing authorities and the Congress want it that way - and if that is the way it is wanted, I feel that is the way it ought to be supplied. In other words, if a given legislator derives more meaning from the budget if certain personnel details are set out at great length, he ought to have those figures as he wants them, so that he can do the best job that he can in review. Other legislators can probably work better with data presented in different form. Although presentation of the data in various forms is expensive, it achieves, even at a cost, one purpose of the budget, that is to make us think. What matters really, to me, is that we are in fact getting the performance budget, because:

The Performance Budget is a common sense tool of efficient administration. It expresses the work programs of government in terms of accomplishment. These terms are understood alike by legislator, administrator, and citizen. That it is consistently understood, is of course the secret of its effectiveness.¹⁰⁰

¹⁰⁰ Contra Costa County Taxpayer's Association. An Approach to the Technique of Performance Budgeting, op. cit.

CHAPTER VI

THE PRESENT NAVY DEPARTMENT PERFORMANCE BUDGET

We have at this time, a performance type budget for the Department of the Navy, as follows:

- (A) Personnel, Military
 - (1) U. S. Navy
 - (2) U. S. Naval Reserve
 - (3) U. S. Marine Corps
 - (4) U. S. Marine Corps Reserve
- (B) Maintenance and Operations
 - (5) General Expenses, Naval Personnel -
[This is for "boot" training,
advanced training, etc.].
 - (6) General Expenses, Marine Corps Personnel
 - (7) Ships and Facilities
 - (8) Ordnance and Facilities
 - (9) Aircraft and Facilities
 - (10) Civil Engineering
 - (11) Medical Care
- (C) Service-Wide Administration
 - (12) Service-Wide Supply and Finance
 - (13) Service-Wide Operations
- (D) Capital Expenditures
 - (14) Shipbuilding and Construction
 - (15) Aircraft and Related Procurement
 - (16) Marine Corps Procurement
 - (17) Public Works
 - (18) Research, Navy¹⁰¹

¹⁰¹Rear Admiral Clextan, U. S. N., Director of the Office of Budget and Reports, Navy Department, talk before Navy Comptrollership Group, George Washington University, Writer's Class Notes, (Washington, D. C.: Dec. 1954).

We thus have a refined performance type budget with a total of 18 appropriations, whereas the Navy Department was not so long ago supported by over sixty appropriations. I have noted a tendency among some students, to feel that the less number of appropriations utilized to support a department, the better their performance budget is. This probably stems from their observation that when fiscal and management responsibility are tied together in a performance budget, the number of supporting appropriations usually decreases. What such a person misses is that it is not merely using less appropriations that puts one on the performance budget, but rather that less appropriations usually follow the marrying of fiscal and management responsibility.

On one occasion a representative of a department with less time in performance budgeting than the Navy, pointed out that his department was supported by less appropriations than the Department of the Navy, thus their program budget was better than that of the Department of the Navy with its eighteen appropriations. What he had missed, probably, (assuming he was serious and not just arguing for arguments sake), was that a program budget was one with individually "priced" programs, functions, or activities, whichever it is desired to call them. The Navy Department, operating on land, on and under the sea, and in the air, would be inclined to require more appropriations, especially inasmuch as "four plus" appropriations are devoted to an autonomous military unit under the Secretary of the Navy, the Marine Corps. The Marine Corps is so placed of course in keeping with the concept

of the balanced fleet - "the bases need a Fleet, but the Fleet needs bases." We could of course go to some single appropriation I suppose, if we were to choose to follow the advocates of the "least number of appropriations," and let us say call the program, "Maintaining Adequate Sea-Power." However, it would be impossible to tie fiscal and management responsibility together as it now is. For example, when the proper size guns were not available for re-gunning a cruiser, the present method of appropriations, performance reports and management responsibility lays the responsibility clearly on the administrator of "Ordnance and Facilities," the Bureau of Ordnance.

It is further noted in the Navy budget, at present, that Military Personnel uses four appropriations. Questions have been raised on this matter, first, regarding the use of so many appropriations, second, for even, under program budgeting, having appropriations for military personnel instead of charging to the other appropriations. It has been explained that we do use four appropriations for facility of handling, and we have separate military Personnel appropriations in the first place because of the multitude of statutes relating to this area. It has further been explained that within the Department of the Navy the cost of military personnel chargeable to each other appropriation, is available.¹⁰² The appropriation for Military Personnel might of course be termed something such as "Manning the Naval Establishment", thus showing it as a function and qualifying it as a program.

¹⁰²Ibid.

CHAPTER VII

LOOKING AHEAD AND THE FUNCTIONAL OPERATING REPORT

There is at least one psychological "gimmick" to program budgeting that we must watch carefully. It is in the presentation of performance data. A department might ask for a total of \$1,000,000 to operate, let us say, an office force that has as sole function the turning out of reports. They show the \$1,000,000 of course in the "object" style, as scattered in pieces of various appropriations. Congress may appropriate the funds totalling \$1,000,000 more because of the press of time, than because of having had the opportunity for a thorough study as to what the funds will do. The next year, going under the program budget, the Department lists this Activity "X", purpose to turn out a certain report, expenditure estimate, \$1,000,000. We have the form of a performance budget, everyone feels we are "on the beam," and we find that the money is appropriated. That year, the activity turns out 100,000 reports, by working no better or no worse than in the previous years. These 100,000 reports of course cost \$10.00 apiece, part of that \$10.00 being caused by wasted time on the job and all other wastage. Next year the activity feels that it will be required to turn out 130,000 reports. It submits its expenditure estimate for 130,000 reports at \$10.00 a

report, for a total requirement of \$1,300,000.00. This figure is based on performance (good, bad, or indifferent), so it may have a magic appeal, and, is approved. My point is, that the magic now attached to the name "performance budget" will, I hope, soon rub off so that reviewers will really get into finding out if the cost of a \$10.00 report shouldn't in fact be about \$4.85 a report. I think that this will come, as more use is made of the performance budget, and as we settle down in our stride under it, and after true performance reporting has been fully obtained.

We have covered the performance type budget, from its first appearance on Staten Island, New York in 1912 up to the present, but we have not discussed an outgrowth of performance budgeting that has the emotional and civic appeal of the performance budget. This outgrowth is called the Functional Operating Report and it is covered in Appendix one, herewith appended, in order to preserve the continuity of this basic paper.

APPENDIX I

THE FUNCTIONAL OPERATING REPORT

The Functional Operating Report, which is also the title of a book by Robert R. Doane and Joseph E. Canning,¹ refers to a format for corporation reporting that has a public relations appeal. The title page in the book succinctly sums the report as being, "The new form of social accounting for use in public and employee relations."²

The Functional Operating Report, commonly called the "Short Form" of report, was apparently conceived in 1937 by the late Orlando F. Weber.³ However, inasmuch as the present accounting philosophy dates back over 500 years, the functional approach has been slow to take hold. In 1942, the American Economic Foundation championed the short form as the most practicable means of attacking the economic and accounting misunderstandings that may have contributed to some wage and labor disputes. An idea of the misunderstandings may be learned from Bradshaw's Developing Men for Comptrollership:

In May, 1946, the Opinion Research Corporation of

¹Robert R. Doane and Joseph E. Canning, The Functional Operating Report, (New York, The American Economic Foundation:1947).

²Ibid., p. 1. ³Ibid., p. 27.

of Princeton, New Jersey, made a nation-wide survey, interviewing a national cross-section of white-collar and manual workers. One of the questions asked was, "Just as a rough guess, what percentage of [sales] would you say the average manufacturer made as profit in peacetime?" 65% of the employees interviewed had opinions about company profits as follows:

- (1) 11% thought profits exceeded 50% of sales.
- (2) 14% thought profits were between 34% and 50%.
- (3) 40% thought profits were 55% or more.

In response to another question, the same group thought that a "fair" profit would be about 10%.According to figures compiled by the National City Bank of New York, net profits of 1017 manufacturing concerns, [expressed] as a percent of sales, was 3.7% in 1944, and 3.3% in 1945...even in 1947, a year of supposedly enormous profits, the Federal Trade Commission report shows that for all manufacturing concerns in the United States, net profits after taxes amounted to 6.7% of sales.⁴

In another survey Opinion Research asked this question, "after a factory has paid for overhead and materials, which would you say gets the bigger share of what is left, stockholders and top management or workers wages?" (Replies are tabulated)

- (1) 64% said stockholders and top management
- (2) 22% said workers wages
- (3) 14% did not reply

Upon examining data from 72 large industrial corporations with assets totaling \$27,000,000,000.00, it was noted that materials, parts, services, etc. accounted for 64.2% of sales dollars. Taxes claimed 6%. The balance of 29.8% of income was available for wages, dividends to owners and wages, and re-investments in the business. To bring these figures down to "earth" and make them more meaningful, the [tabulation for the General Motors Corporation for the year 1945 is set forth]:

⁴T. F. Bradshaw, Developing Men for Comptrollership, (Cambridge, Mass., Harvard University Press: 1950), p. 214.

Of 29.8% available as above

- (1) .4% for salaries - directors, officers and top executives.
- (2) 83.9% to other salaries.
- (3) 11.8% Dividends to owners.
- (4) 3.9% re-invested in business.⁵

Before proceeding I must point out that the 11.8% dividend figure is of course not 11.8% of sales, but is rather, 11.8% of 29.8% of sales, or about 3.5% of sales dollars.

Now just exactly where such opinions can and do take us, is well shown by a report in a recent edition of the Wall Street Journal:

These High School Pupils are Leery of Capitalism. By a Wall Street Journal Staff Reporter.

Boston - (December 8, 1954) - The profit incentive is not essential to the survival of the American free enterprise economic system. The best way to raise living standards is for workers to get more of a company's income. One or two companies in many industries almost monopolize these industries.

These were some of the responses by high school seniors in 86 schools scattered throughout the United States as disclosed in a poll on attitudes toward the free enterprise system, conducted by the United States Chamber of Commerce. They were disclosed here by Paul H. Good, Manager of the education department of the Chamber and one of a number of speakers at an "Explaining Your Business" meeting conducted by the Greater Boston Chamber of Commerce.

Mr. Good said 82% of the seniors "just don't believe we have competition in our business world." Six of ten said owners get too much of the money that business makes, and three out of four said that most of the gains from new machinery go to the owners and not workers.The survey

⁵Ibid., p. 215.

found 55% of the students agreed with the communist theory "from each according to his ability, and to each according to his needs."⁶

Underscoring is mine. I am startled by the report. What side would this 55% be on if we suffered another depression? And this is what the misinformation about business has brought us, a confused group of high school seniors who claim on one hand that we have ended up with a few companies surviving in a field, (from competition), yet on the other hand claiming that there is no competition in American business!

Until fairly recently, income and operating statements of corporations were of interest only to owners and top management. These people either understood the language and figures, or they employed trained interpreters. In later years however, the nation's "social conscience" has brought about sociological changes in labor and public relations that have made it desirable to make operating reports available to the workers and general public.

The public and labor, and others probably had the same dilemma described by Mr. Fred V. Gardner in his work Variable Budget Control, as he explained in the introduction to the book, the troubles that he, a trained accountant, encountered in trying to reconcile that a unit which cost \$5.00 to manufacture was sold at a loss at \$7.50.⁷

⁶Wall Street Journal, December 8, 1954.

⁷Fred V. Gardner, Variable Budget Control, (New York, McGraw-Hill Book Company: 1946), p. ii.

However, the same vocabulary that confounded Mr. Gardner, was the system and vocabulary then offered to the public and labor. The technical terminology of the accounting profession was jammed into a service for which it was not intended. These new consumers were interested but they could not understand it, hence the growth of the myth of excessive profits and a growing distrust of the private enterprise system to the extent reported in the Wall Street Journal as quoted above.

The American Economic Foundation has researched extensively into the semantics of corporate operating reports. It is felt that the "Short Form" places the story of "who gets how much for doing what", in simple format for presentation to the public in terms that cannot be confused by accident or intent.

There have been workers who have gone on strike to enforce wage demands that were arithmetical impossibilities, but if the worker tried to verify union claims of excessive profits he might encounter great difficulties. He would find no payroll total. A search for "The Profit" would find at least four types of profits mentioned.

In the "Short Form" there is only one entry for profits. Yet the Functional Report need only be another form of report, with the conventional forms of reports becoming subsidiary thereto, yet still available for business and financial needs. The "Short Form" is the laymen's articulate edition of the more lengthy profit and loss statement of the professional accountants. Its use does not necessitate any change to the present established

methods or vocabulary of accounting. It does not replace the conventional report, it merely supplements it.

In the usual income statement of a company, the residue left after all costs have been met is merely regarded as profit. The impression usually conveyed, is that the tools and plant employed in production made no contribution to production, and hence those who made the tools possible will continue to do so. In the Functional Report, profit is clearly identified as "Cost of Using the Tools." It is shown as a cost of production paid to owners to get them to supply the tools and plant.

The Functional Report emphasizes fundamentals:

- (1) The customer, by his volume of purchases and the price he will pay, fixes the whole manufacturing structure down to wages.
- (2) It is the customer who pays corporation taxes.
- (3) Dividends are paid as a cost of operation to get someone to provide the tools required.

Appended herewith is a typical income statement, shown first in conventional form, and next in the "Short Form."

The "Short Form" has been known for several years now, but its essence has been slow in creeping into corporation reports. I picked up thirty-two reports of typical U. S. Manufacturing Corporations and found:

- (1) Reports of six Corporations⁸ used "pie charts" to show

⁸Annual Reports: Safeway Stores, 1953; Western Union, 1953; Bell Aircraft, 1953, Union Pacific, 1953; New York Central, 1953; General Mills, 1953.

where the "sales dollar went." It was usually evident what amount went for raw materials, for labor, for taxes, for depreciation, for future development, and to stockholders.

(2) Two of the reports⁹ used a practice of adding "Net Profit for Year" to "Balance of Profit Employed in Business at beginning of Year", and coming up with a large figure which in each case was left unlabeled. A glance might cause a layman reader to carry off some gross erroneous profit figures.

(3) One report¹⁰ clearly labelled an amount as, "Share Owners' cash dividends paid for the use of their money invested in the business."

(4) Eight reports¹¹ clearly priced wages, salaries, social security, taxes and pensions.

(5) Fifteen Reports utilized the conventional profit and loss format and usually lumped many costs into "cost of goods sold" and generally gave more space to discussion of dividends.

In spite of the fact that some Functional Reporting is appearing, I feel we need a lot more of it. Especially in view of the article in the Wall Street Journal.

⁹Annual Reports: Proctor & Gamble, 1953; Caterpillar Co., 1953.

¹⁰Annual Report, Union Oil Co., 1953.

¹¹Annual Reports: Harbison-Walker Refractories; 1953; RCA, 1953; Colorado Fuel and Iron Corp., 1953; Sohio, 1953; Allegheny Ludlum Steel, 1953; Corn Products Refining, 1953; West Virginia Pulp and Paper Co., 1953; Westinghouse, 1953.

TYPICAL INCOME STATEMENT

("Control" Accounting)

Gross Sales	\$982,400
Less returned sales and allowances	<u>13,260</u>
Net Sales	\$969,140(A)

COST OF GOODS SOLD:

Manufacturing Expense:

Direct materials used	\$246,184(B)
Factory supplies	35,957(B)
Direct labor	203,101(C)
Indirect labor, including plant clerical wages	53,956(C)
Depreciation, depletion and obsolescence	40,855(D)
Amortization of Emergency Facilities	5,230(D)
Taxes on plant	<u>30,177(E)</u>

Total cost of goods sold \$615,460

Gross Profit on Sales	\$353,680
Salesmen's salaries	49,890(C)
Traveling expenses	20,310(B)
Advertising	25,525(B)
Postage used in selling	5,850(B)
Dealer service	25,700(B)
Freight, out	43,130(B)
Cartage and outside storage	5,710(B)
Motor vehicle registration fees	<u>2,135(E)</u>

Total selling expenses \$178,250

Net Profit on sales \$175,430

GENERAL AND ADMINISTRATIVE EXPENSE:

Officers salaries	\$ 25,000(C)
Office clerical salaries	15,900(C)
Labor Pension Plan payments	6,870(C)
Social Security tax payments	9,820(C)
Legal and auditing expense	6,410(B)
Rent	4,000(B)
Stationery and office supplies	3,200(B)
(documentary stamps)	(400)(E)
Telephone and telegraph	3,744(B)
(communication tax)	(936)(E)
Insurance	1,247(B)
Amortization	<u>1,248(D)</u>

Total general and administration expense \$ 78,775

Net Profit on Operations \$ 96,655

TYPICAL INCOME STATEMENT
(continued)

OTHER INCOME:

Dividends received	\$ 1,750
Interest on government bonds	<u>400</u>

(Total non-operating profit)	\$ 2,150*
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Total operating and non-operating profit	\$ 98,805
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FINANCIAL EXPENSE (net:)

Discount given on sales	\$ 10,565(A)
Bond interest	4,970(B)
Other interest	<u>1,680(B)</u>

Total financial expense	\$ 17,215
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Net Profit before income taxes	\$ 81,590
Less Income and Profits Taxes	<u>12,065(E)</u>

Net Profit or Income	\$ 69,525(E)
Less Dividends Paid	<u>39,375</u>

Surplus	\$ 30,150
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* subtract from (F), report in (G)

Same statement reduced to
FUNCTIONAL OPERATING REPORT
("Social" Accounting)

(A) WE RECEIVED FROM CUSTOMERS \$958,575(100%)

THESE RECEIPTS WERE EXPENDED FOR:

(B) The Cost of Goods and Services
Bought from Others \$433,617(46%)

(C) The Cost of Human Energy
(Wages and Salaries) 364,537(38%)

(D) The Cost of Tools Wearing Out
(Depreciation, Depletion) . 47,333(5%)

(E) The Cost of Payments Ordered
By Government (Taxes) . . . 45,713(4%)

(F) The Cost of Using the Tools
(Profit) 67,375(7%)

TOTAL EXPENDED \$958,575(100%)

(G) The corporation also received \$2,150 that was
not related to the manufacture or sale of its
product.

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